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SUBJECT: Central Bank Governor Firm on Independent Policies

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¶1. (SBU) Once again showing his readiness to speak out in implied criticism of government policies and to assert his independence in monetary policymaking -- including in an election year -- Central Bank Governor Durmus Yilmaz told a conference in Istanbul March 7 that the inflation rate was not acceptable at its current level. He said it was not yet time to relax monetary policy and that the government should continue to implement structural reforms and prudent fiscal policies.

¶2. (SBU) In his speech to the "Risk Management Summit", organized by Active Academy and Zaman newspaper, Yilmaz maintained that structural, "microeconomic" reforms are required to ensure price, and thus macroeconomic, stability. Yilmaz stressed that in an environment in which price stability is not maintained, social and economic distortions inevitably arise. Yilmaz explained that Central Bank policy aim at maintaining price stability via inflation targeting and encouraging a healthy economic environment in which individuals and firms are confident to save and invest. "In other words, the struggle against inflation means the effort to strengthen the decision making process," he said.

¶3. (SBU) Claiming that significant steps have been taken on the path to the price stability over the last five years, Yilmaz pointed to the 58.3 point fall in inflation since 2002 and noted that fluctuations in the price level have disappeared to a large extent. He said that the flexible exchange rate regime has made great contributions to the adoption of modern risk management principles in Turkey. He added, "Exchange rate risk is beyond the control of economic institutions. And this fact, as the Central Bank states at every turn, makes the exchange rate a risk factor that should be managed."

¶4. (SBU) Yilmaz went on, saying that reforms taken so far are not sufficient. "First of all, price stability is not yet secured. Besides, the inflation rate is not yet low enough to be neglected in the decision making process of economic institutions. This is the issue I want you to pay attention to: the support of the business community and the public was very important in the effort through which the inflation rate was reduced from high figures to single digits. The continuation of this support remains very important as well... Our target is at least as far away as the distance we have made so far." said Yilmaz.

¶5. (SBU) Comment: This is not the first time that the Governor has spoken out against complacency or to affirm the independence of the Turkish Central Bank from political pressure. Especially given the doubts in the marketplace that accompanied his appointment last year, his willingness to speak out in defense of sound policies is refreshing. Government ministers including Prime Minister Erdogan, Finance Minister Unakitan and Economy Minister Babacan continue to make comments that arguably encroach on the Central Bank's turf, such as calling for lower interest rates or commenting on the

inflation target. There are persistent rumors, including in the press, that the AKP-led government is not happy with his outspokenness and is even looking for ways to entice him to leave office, such as by offering him an ambassadorship in a Turkish embassy abroad. The Governor's five-year term expires in 2011.

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